



Government Contracts

The SBA, Mandatory Disclosure & You – HOT OFF THE PRESSES



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Agenda

- Introduction
 - The Speakers
- The Small Business Administration Contract Assistance Programs
 - What is a “small business”
 - Don't forget the VA's VIP Program
 - Affiliation
 - Mentor-Protégé – All Small & 8(a)
 - Exposures
 - Are you small?
 - Do you certify yourself as small?
- The Mandatory Disclosure Rule
 - False Claims Act Liability
 - Implied Certification & FCA Liability

Introductions



Adele Navarrete
Senior Corporate Counsel, LMI

Adele Navarrete is Senior Corporate Counsel at LMI.

- Adele has over ten years combined experience in law firm and in-house practice with a focus on government contracts.
- LMI has almost 60 years experience providing government management consulting helping the federal government solve its toughest problems.

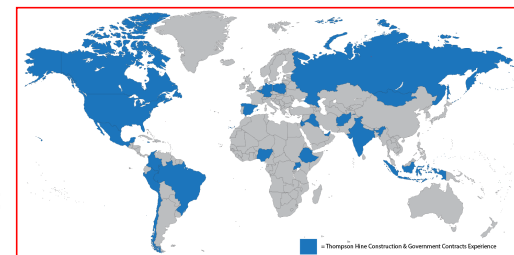
Adele received her law degree from University of Michigan Law School.



Larry Prosen
Partner, Kilpatrick Townsend

Larry Prosen is a government contracts attorney who holds a degree in architecture and has specialized in construction litigation.

- Practiced Construction Litigation and Government Contracts for 23+ years.
- Litigated claimed and disputes across the U.S. and around the world.
- Hundreds of Miller Act and private bond disputes; Bid Protests, Claims, Internal Investigations; Compliance Reviews & SBA Size & Status Protests/Issues.



Larry received his law degree from Catholic University of America Columbus School of Law and his undergraduate degrees in Architecture and History from University of Maryland.

SBA's Alphabet Soup

■ Federal Level

- 8(a) – Socially or Economically Disadvantaged SBC
- WOSB – Woman-Owned Small Business Concern
- SDVO SBC – Service-Disabled Veteran-Owned SBC
- HUBZone – Historically Underutilized Business Zone SBC
- SBC – Small Business Concern
- VIP – Department of Veteran's Affairs

■ State Level (federal implications)

- DBE – Disadvantaged Business Enterprise
- WBE – Woman-Owned Business Enterprise
- MBE – Minority-Owned Business Enterprise

Socioeconomic Policies (FAR Part 19)

- Everyone wants a piece of the pie – their “fair” share!

- Small Businesses
- Small Disadvantaged Businesses/8(a)s
- HUB Zone
- Women-Owned
- ANCs (Alaska Native Corporations), Tribal Entities
- Veteran-Owned
- Service-Disabled, Veteran-Owned

**Different
Categories
May Have
Different
Evaluation
Processes**

- Contracting agencies have “goals”

Know Who You Are and Where You Fit In

What Happens If You Don't Meet Your “Goals”? (FAC 2005-94)

Who is “Small”? How Determined?

- “Small” is determined by either the average annual revenue of the entity over the past 5 years (changed from 3 years in August 2019) or the number of employees – Small Business Runway Extension Act.

<https://www.kilpatricktownsend.com/en/Blog/governmentcontracting/2019/12/SBA-Finalizes-Small-Business-Runway-Extension-Act-Regulations-Small-has-a-new>

<https://www.kilpatricktownsend.com/en/Blog/governmentcontracting/2019/7/Small-Businesses-Can-Now-be-a-Little-Larger-Under-the-SBAs-Increased-Size-Standards>

- 13 C.F.R. Parts 121 & 124.
- 8(a) & WOSB require SBA or VA certification.

13 C.F.R. §121.104 – Calculating Annual Receipts

(a) *Receipts* means **all revenue in whatever form received or accrued from whatever source**, including from the sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances. Generally, receipts are considered “total income” (or in the case of a sole proprietorship “gross income”) plus “cost of goods sold” as these terms are defined and reported on Internal Revenue Service (IRS) tax return forms....For size determination purposes, the only exclusions from receipts are those specifically provided for in this paragraph. All other items, such as subcontractor costs, reimbursements for purchases a contractor makes at a customer's request, investment income, and employee-based costs such as payroll taxes, may not be excluded from receipts.

(1) The Federal income tax return and any amendments filed with the IRS on or before the date of self-certification must be used to determine the size status of a concern. SBA will not use tax returns or amendments filed with the IRS after the initiation of a size determination.

(2) When a concern has not filed a Federal income tax return with the IRS for a fiscal year which must be included in the period of measurement, SBA will calculate the concern's annual receipts for that year using any other available information, such as the concern's regular books of account, audited financial statements, or information contained in an affidavit by a person with personal knowledge of the facts.

13 C.F.R. §121.104 – Calculating Annual Receipts

(c) *Period of measurement.* (1)...annual receipts of a concern that has been in business for 5 or more completed fiscal years means the total receipts of the concern over its most recently completed 5 fiscal years divided by 5. For certifications submitted on or before January 6, 2022, rather than using the definitions in this paragraph (c), a concern submitting a certification may elect to calculate annual receipts and the receipts of affiliates using either the total receipts of the concern or affiliate over its most recently completed 5 fiscal years divided by 5, or the total receipts of the concern or affiliate over its most recently completed 3 fiscal years divided by 3.

(2) Except for the Business Loan and Disaster Loan Programs, annual receipts of a concern which has been in business for less than 5 complete fiscal years means the total receipts for the period the concern has been in business divided by the number of weeks in business, multiplied by 52.

(d) *Annual receipts of affiliates.* (1) The average annual receipts size of a business concern with affiliates is calculated by adding the average annual receipts of the business concern with the average annual receipts of each affiliate.

(2) If a concern has acquired an affiliate or been acquired as an affiliate during the applicable period of measurement or before the date on which it self-certified as small, the annual receipts used in determining size status includes the receipts of the acquired or acquiring concern. This aggregation applies for the entire period of measurement, not just the period after the affiliation arose. However, if a concern has acquired a segregable division of another business concern during the applicable period of measurement or before the date on which it self-certified as small, the annual receipts used in determining size status do not include the receipts of the acquired division prior to the acquisition.

Who is “Small”? How Determined? – NAICS

- For R&D, Manufacturing, etc. – looks at annual number of employees
- For most other trades, entities, looks at average annual revenue over the past 5 years –

SMALL BUSINESS SIZE STANDARDS BY NAICS INDUSTRY			
NAICS codes	NAICS U.S. industry title	Size standards in millions of dollars	Size standards in number of employees
Subsector 517—Telecommunications			
517311	Wired Telecommunications Carriers		1,500
517312	Wireless Telecommunications Carriers (except Satellite)		1,500
517410	Satellite Telecommunications	\$35.0	
517911	Telecommunications Resellers		1,500
517919	All Other Telecommunications	\$35.0	
Subsector 518—Data Processing, Hosting, and Related Services			
518210	Data Processing, Hosting, and Related Services	\$35.0	
Subsector 519—Other Information Services			
519110	News Syndicates	\$30.0	
519120	Libraries and Archives	\$16.5	
519130	Internet Publishing and Broadcasting and Web Search Portals		1,000
519190	All Other Information Services	\$30.0	

Affiliation – A Major Pitfall

- §121.103 How does SBA determine affiliation?

(a) General Principles of Affiliation. (1) Concerns and entities are affiliates of each other when one controls or has the power to control the other, or a third party or parties controls or has the power to control both. It does not matter whether control is exercised, so long as the power to control exists.

(2) SBA considers factors such as ownership, management, previous relationships with or ties to another concern, and contractual relationships, in determining whether affiliation exists.

(3) Control may be affirmative or negative. **Negative control includes, but is not limited to, instances where a minority shareholder has the ability, under the concern's charter, by-laws, or shareholder's agreement, to prevent a quorum or otherwise block action by the board of directors or shareholders.**

(4) Affiliation may be found where an individual, concern, or entity exercises control indirectly through a third party.

(5) In determining whether affiliation exists, SBA will consider the totality of the circumstances, and may find affiliation even though no single factor is sufficient to constitute affiliation.

(6) In determining the concern's size, SBA counts the receipts, employees, or other measure of size of the concern whose size is at issue and all of its domestic and foreign affiliates, regardless of whether the affiliates are organized for profit.

Affiliation – Types/How Found?

- Common Stock Ownership – 50% or more of controlling ownership interest
- Stock Option, Convertible Notes, and Merger Agreements
- Common Management
- Identity of Interest – 2 or more family members in identical or substantially identical business or economic interests or economically dependent –
 - Spouses, parents, children, siblings presumed to be affiliated – if they conduct business together – overcome presumption via a clear line of fracture

Affiliation – Types/How Found?

- Newly Organized Concern – former officer, director, stockholder, managing member, or key employees – same or related line of business or industry
- Joint Venture – 3 in 2 rule & both must be small or mentor/protégé
- Ostensible Subcontractor – overdependence
- **STANDARD IS: TOTALITY OF THE CIRCUMSTANCES so Affiliation can be found other ways.**

Affiliation – Limited Exceptions

- 13 C.F.R. § 121.104(b) – A number of exceptions, including:
 - ANCs, Native American-Owned Entities
 - Joint Venture of two or more small businesses where each are small
 - SBA-approved Mentor-Protégé Program
 - Recognized financial/investment-type company
 - Common administrative services – accounting, etc., IF proper payment – a formal management services arrangement

Joint Venture Exception

3) *Exception to affiliation for certain joint ventures.*

(i) ***Each concern is small*** under the size standard corresponding to the NAICS code assigned to the contract.

(ii) ***Two*** firms ***approved by SBA as mentor and protégé*** under §125.9 can joint venture as a small business for any Federal government prime contract or subcontract –

- Protégé must qualify as small for the size standard corresponding to the NAICS code assigned to the procurement, and the other joint venture requirements of §§124.513(c) & (d), §§125.8(b) & (c), §§125.18(b)(2) & (3), §§126.616(c) & (d), or §§127.506(c) & (d) of this chapter, as appropriate.

JVs – The Mentor/Protégé Program

- Started as 8(a) – expanded to all SBA assistance programs in 2016 - Two programs combined:
 - 8(a)
 - All Small – Small, WOSB, HUBZone, SDVO SBC
- Allows a large business to “team” with a small business and gain access to small business contracts.
- This is the only way that a large business can gain access to small business set aside programs – certainly as prime & then watch out for overdependence and ostensible subcontractor rule.

Mentor-Protégé

Two firms **approved by SBA** to be a mentor and protégé under §124.520 may JV as a small business for any Federal government prime contract or subcontract, provided:

1. Protégé qualifies as small for the corresponding NAICS code size standard assigned to the procurement.
2. In the case of 8(a) sole source requirements, has not reached the dollar limit set forth in §124.519 of these regulations.
3. SBA Approval - If 8(a) BD program award - SBA must approve the joint venture pursuant to §124.513.
4. If other than 8(a), SBA need not approve the JV prior to award, but if JV size status is protested, the provisions of §§124.513(c) and (d) will apply.

Mentor-Protégé

§125.9 What are the rules governing SBA's small business mentor-protégé program?

General. Mentor must provide “mentorship” to the protégé – can include technical and/or management assistance; financial assistance in the form of equity investments and/or loans; subcontracts (either from the mentor to the protégé or from the protégé to the mentor); trade education; and/or assistance in performing prime contracts with the Government through joint venture arrangements.

The Mentor

(b) *Mentors*. Typically large but can be a small business if the concern can demonstrate that it

- (i) Is capable of carrying out its responsibilities to assist the protégé firm under the proposed mentor-protégé agreement;
- (ii) Possesses good character;
- (iii) Does not appear on the federal list of debarred or suspended contractors; and
- (iv) Can impart value to a protégé firm due to lessons learned and practical experience gained or through its knowledge of general business operations and government contracting.
- (v) Mentor generally one protégé at a time, but there are exceptions of up to three protégés at a time.

The Protégé

Protégés. Must be small based on its primary NAICS code or identify it's seeking business development assistance with respect to a secondary NAICS code and qualify as small for the size standard corresponding to that NAICS code.

(i) May self-certify it is small for its primary or identified secondary NAICS code – there are exceptions if only small under secondary code – firm must show logical business progression of the firm by using the M-P Program.

(2) Protégé generally may only have mentor at a time. SBA may approve a second mentor where the second relationship will not compete or conflict with the first mentor-protégé relationship and:

(i) The second relationship pertains to an unrelated NAICS code; or

(ii) The protégé firm is seeking to acquire a specific expertise that the first mentor does not possess.

Mentor-Protégé – So What? BENEFITS!

Benefits. (1) Protégé and mentor may JV as a small business for any government prime contract or subcontract – so long as protégé qualifies as small for the procurement.

JV may seek any type of small business contract (i.e., small business set-aside, 8(a), HUBZone, SDVO, or WOSB) for which the protégé qualifies.

(i) SBA must approve the mentor-protégé *agreement* before the two firms may submit an offer as a joint venture on a particular government prime contract or subcontract in order for the joint venture to receive the exclusion from affiliation.

(ii) To receive affiliation exclusion, the JV must meet the requirements set forth in §125.8(b)(2), (c), and (d).

Mentor-Protégé – So What? BENEFITS!

- To raise capital, the protégé may sell or otherwise convey to the mentor an equity interest of up to 40% in the protégé.
- No determination of affiliation or control may be found between a protégé firm and its mentor based solely on the mentor-protégé agreement or any assistance provided pursuant to the agreement. However, affiliation may be found for other reasons set forth in §121.103 of this chapter.

Mentor-Protégé – Other Requirements

- Must enter into (a) a compliant M-P Agreement and (b) get it approved in advance by SBA.
- Must file annual reports.
- Must file final report.

HOT OFF THE PRESSES – 222 Pages of Fun

- Final Rulemaking – Scheduled to be published on Fed. Reg. on 10/16/20
- MERGES ALL M/P PROGRAMS INTO ONE PROGRAM.
- Eliminates requirement that 8(a) Participants seeking to be awarded an 8(a) contract as a JV submit the JV Agreement to SBA for review and approval prior to contract award.
- Revises several 8(a) BD program regulations to reduce unnecessary or excessive burdens on 8(a) Participants.
- Clarifies other related regulatory provisions to eliminate confusion among small businesses and procuring activities.
- Requires a business concern to recertify its size/socioeconomic status for all set-aside orders under unrestricted MACs, unless contract authorized limited pools of concerns for which size and/or status was required.

HOT OFF THE PRESSES – Updated Regulations

- M/P – Identify of Interest if Protégé gets 70% of business over the past three years from Mentor – now rebuttal presumption by showing a lack of sole dependence – particularly with newly formed entities.
- Newly Organized Concern – Now adds former or “current” key employees, shareholders, members, etc.
- Joint Venture – Intended to not be a separate entity
 - Lasts 2 years from date of first award and then can form a new JV –
 - If offer (with price) made within two year period – can get award and perform after 2 years expires – no need for a novation.
 - JV may have its own administrative personnel (e.g., FSO) but not have own employees perform the work.
- MACS – Different provisions for set-aside and open competition efforts.

<https://public-inspection.federalregister.gov/2020-19428.pdf>

Small Business Set-Asides – Exceptions (FAR Part 19)

- The Rule of 2 - No responsible small businesses (*i.e.*, unlikely to receive 2 or more offers from a responsive, responsible small business)
 - Market Research
- Outside of U.S.

All Methods of Acquisition Are Fair Game

HOT OFF THE PRESSES: WOSB & EDWOSBs

EFFECTIVE OCTOBER 15, 2020:

- NEW APPLICANTS: WOSBs & EDWOSBs must be certified either by SBA through its 8(a) program, a third-party certifying entity or the VA's CVE Program.
 - Applies to entities both individually and as part of IDIQ/Pools
- SELF-CERTIFIED
 - ACTIVE CONTRACTS: Firm eligible at time of contract as WOSB or EDWOSB is considered one for life of the contract
 - If contract life is over 5 years (including options) must become certified by SBA or approved third party certifier prior to end of 5th year.
 - NO ACTIVE CONTRACTS: Must be formally certified by SBA
- 8(a) & CVE Firms – can upload most recent SBA 8(a) annual review or acceptance letter if in year 1
- Beta.certify.sba.gov
 - Even if third-party certified still need an account.

NOTE: Those WOSBs that previously filed on certify.sba.gov must refile their documents related to WOSB certification at beta.certify.sba.gov

The VA & VIP Program

- To perform as a small business for the VA, needed to be formally certified by the VA as “VIP” – part of the Vets First Verification Program.
 - Vets First Verification Program affords verified firms **owned and controlled by Veterans and Service-disabled Veterans** the opportunity to compete for VA set asides. During Verification, the Center for Verification and Evaluation (CVE) verifies SDVOSBs/VOSBs per CFR Title 38 Part 74 and 13 CFR Part 125 that address Veteran eligibility, ownership, and control.
 - To qualify for participation in the Veterans First Contracting Program, eligible SDVOSBs/VOSBs must first be verified.
- SBA is now taking over the administration of that program as to Ownership & Control Issues.

<https://www.kilpatricktownsend.com/en/Blog/governmentcontracting/2018/1/VA-looks-to-SBA-for-Future-VeteranOwned-Small-Business-Certification>

Veteran-Ownership – 5 Elements

- 2018 SBA rule reconciled differing ownership standards held by SBA and VA
- SBA now recognizes the following “extraordinary instances” where an SDVOSB owner will not have full control over the concern’s decision-making process
 1. Adding a new equity stakeholder
 2. Dissolution of the company
 3. Sale of the company
 4. The merger of the company
 5. Company declaring bankruptcy

Small Business Subcontracting Plans

- FAR 19.704 sets forth plan requirements and applies to contracts with subcontracting potential over \$750,000 (\$1.5M for construction)
- Subcontracting plan is a material term of a contract
- Contractor entitled to *good faith* reliance on representations of subcontractors' size and socioeconomic status
- Failure to exercise good faith can result in liquidated damages *AND* FCA liability
- FCA Liability
 - Claiming small business credit for subcontract where small subcontractor is acting in a pass-through capacity
 - *U.S. ex rel. Savage v. Wash. Closure Hanford LLC*, 2017 WL 3667709 (E.D. Wash. Aug. 24, 2017)

SBA-Related Lessons to Learn

- Small business must have real:
 - Majority ownership
 - Day-to-day and long term control
 - Not be a sham or strawman
 - Bonding Capacity
 - Must be small – be careful if you get close to the size standard
- Must be set up to do work with the government, as applicable:
 - Accounting
 - Training
 - Paperwork
 - Knowledge & Experience



The Mandatory Disclosure Rule

The Mandatory Disclosure Rule – FAR 52.203-13

- 2008 – FAR added the Mandatory Disclosure Rule (MDR):

Requires the “...timely disclosure, in writing, to the agency OIG, with a copy to the Contracting Officer, whenever, in connection with the award, performance, or closeout of any Government contract performed by the Contractor or subcontractor thereunder, the Contractor has credible evidence that a principal, employee, agent or subcontractor of the Contractor has committed a violation of Federal criminal law involving fraud, conflict of interest, bribery or gratuity violations found in Title 18 U.S.C. or a violation of the civil False Claims Act (31 U.S.C. §§ 3729-3733.” FAR 52.203-13(c)(2)(ii)(F).”

- FAR clause is vague and highly nuanced – forcing the ABA to publish a 230-page-plus Guide to the “MDR” in 2009.
 - It is still vague.

Principals and the Mandatory Disclosure Rule

- MDR is couched in the form of a Principal's responsibilities and their exposure in the MDR process.
 - A *knowing* failure by a *principal* to timely disclose credible evidence to the USG of certain misconduct or significant overpayment *known to the principal* results in a violation of the MDR.
 - Can subject the Principals or the firm to suspension and debarment for failure to disclose – and criminal or civil actions.
 - Who is a Principal?

Principal means an officer, director, owner, partner, or a person having primary management or supervisory responsibilities within a business entity (e.g., general manager; plant manager; head of a division or business segment; and similar positions).

Mandatory Disclosure – What's Required?

Compliance with both FAR 52.203-13 & FAR Subpart 9.4

- Credible Evidence of:
 - Criminal violations
 - False Claims Act
 - Significant Overpayments
- Must have within 90 days of contract - Code of Business Conduct and Ethics
 - Unless Small Business – but recommend you have any way
- Internal Controls
 - Code; training, distribution, audits and testing
- Disclosures to OIG/CO

MDR Requirements

- Contractor **must**
 - *timely disclose*
 - *in writing* to the **agency OIG**, with a *copy to the Contracting Officer*,
 - when, in **connection** with the award, performance, or close-out of a **contract or any subcontract** thereunder,
 - the contractor has **credible evidence**
 - that a **principal**, employee, agent, or subcontractor
 - has committed a **violation** of Federal criminal law involving fraud, conflict of interest, bribery or gratuity violations in Title 18 U.S. Code or a violation of the civil False Claims Act.
- Each of these elements is vague & open to interpretation.
- DOES allow time for an internal investigation – but how much time?

What Steps Should You Take Upon Learning of a Possible Violation?

- A. Perform Initial Due Diligence
 - Did the system work? How did it not?
 - What was the context in which the alleged violation happened?
- B. Engage outside counsel – Privilege and Independence is Key
- C. Conduct Internal investigation
 - Maintain Attorney-Client Privilege
 - Form a Special Committee?
 - Develop findings and if necessary plan for communicating with the USG
 - Document/data preservation – Litigation Hold - Enron
 - Employee interviews – Conducted by outside counsel – UPJOHN WARNING!
- D. Consider potential collateral consequences
 - Insurance issues
 - Disciplinary Actions & Lessons Learned/Fix the Problem
- E. Planning on how to defend the case
- F. Negotiations with the Government – Fines, Penalties, Suspension, Debarment?

Some Higher Contractor Risk/Exposure Areas

- The News Worthy Classics

- Time charging – over charges
 - SCA/DB Act Violations
- Defective products or services

- False Certifications

- Statutory and FAR Mandated Certifications – Pay Applications, Certified Payrolls
- Small Business Certifications – Special areas of risk in the SBA's contracting programs:
 - 13 C.F.R. 121.108 – small business set-asides
 - Consequences of numerous SBA filings and forms
- Implied certifications – *Escobar*

Recent Trends Over the Past 5 Years

■ Recent Trends:

- *Escobar* fallout – Implied certifications leading to FCA liability
- Ethics and Compliance Programs are Essential & Mandatory
- Mandatory Disclosure Rule and its relation to the FCA
- Internal Investigations and Whistleblower Protections – Need to have contingency plans for the former and protections in place for the latter

***De Minimus* Internal Control System – FAR Requirements**

- WHEN DO I NEED AN ETHICS CODE?
- FAR 52.203-13 requires this in all contracts exceeding \$5 million or 120 days (commercial item contracts excluded) – \$5 million individually or in the aggregate.
 - Mandates written Code of Government Contractors Business Ethics and Conduct.
 - **Must** be provide/accessible to every employee working on that contract.
 - Contractor must diligently promote and pursue compliance to both (a) prevent and (b) detect criminal conduct
 - Create an organizational culture that encourages ethics and compliance.
- Other Requirements:
 - Assign responsibility at a sufficiently high level and provide adequate resources.
 - Screen individuals potentially involved in improper conduct.
 - Perform periodic compliance reviews & audits of procedures, policies and internal controls – does the system work? Tests?
 - Allow for an anonymous internal reporting mechanism such as a hotline.

***De Minimus* Internal Control System – FAR Requirements**

- Develop & Provide a process for handling incidents/violations, investigations and reports to the USG.
- Periodic Education & Training.
- Appropriate disciplinary action for (a) violation and (b) failing to report or prevent misconduct.
 - Should have a zero-tolerance policy for retribution or retaliation.
- Timely disclosure of violations – MANDATORY!
- Fully cooperate with USG audits, investigations & corrective actions.
- Suggest that you take the initiative – we are already taking action or corrections...

Some MDR Takeaways

■ Practice Pointers:

- Even if a determination is made to NOT make an MDR report of an alleged incident that implicates offenses enumerated in the MDR, document the basis for that decision.
- Consider the extent of Principals' involvement in the event and investigation – granting Principals with knowledge of, and access to, a potentially reportable incident puts them and the company at risk.
- To what extent do your Principals participate in the MDR reporting decision – what happens if two (or more) Principals disagree about whether a MDR report should be filed???
- Recommended that Contractors should have an MDR policy – who leads, who decides on whether to report and MDR event, etc.?
- Most importantly, internal investigators must be aware of the MDR and conduct investigations in a manner that allows the MDR requirements to be met and documented.

- Question: How does one balance the “credible evidence” reporting trigger with FAR (and likely DOJ) demands for “full disclosure”? This may require incremental reporting and requires you to be clear about the context & limitations of your initial report.



Escobar & Implied Certification

Implied Certification & FCA Liability

- ALL Government Contractors or projects receiving Federal Monies need to be careful
 - False Claims has become a MAJOR area of oversight
 - Express – Pay Apps; Size Status & Certified Claims
 - Implied – SBA/DBE/MBE & Specification Compliance Issues
 - U.S. Government has tried implied certifications for years – they now have traction.

Hot Topic – False Claims Act & Certifications

- Over the past decade, significant uptick in FCA claims
 - Over \$3 billion recovered by DoJ in 2019 (down from \$4.7 billion in 2016)
 - Also holding individuals liable
 - False Certifications – Fraudulent claims, pay applications, SBA/DBE certifications
 - 3rd Circuit rejects appeal on \$136 million scheme to secure highway construction contracts meant for MBEs in Pennsylvania – President sentenced to 84 months plus \$1 million in fines;
 - Platinum One – Husband and wife sentenced to 5 years for fraudulently seeking SBA HubZone contracts and filing false tax returns;
 - L-3 pays \$25.6 million for defective weapons sights;
 - Walgreens to pay \$9.9 million for Medi-Cal Billing FCA suit.

False Claims Act – So what?

- My company doesn't do federal work, why should I care?
- Can extend to state and local contracts with federal financing.
- Many states have state/local equivalents.
- Suspension & Debarment at one level and extend to other levels.
- Not just corporate exposure, can be individual too.

Guidelines – What is Materiality?

- Court's mentioned guidelines:
 - Misrepresentation is not automatically material just because the Government designates compliance with a particular requirement as a condition of payment;
 - Just because the Government may have the option to decline payment if it had knowledge of a noncompliance does not automatically result in a finding of materiality;
 - Materiality does not exist if a noncompliance is minor or insubstantial;
 - Evidence that a defendant knows the Government “consistently refuses to pay claims in the mine run of cases based on noncompliance with the particular statutory, regulatory, or contractual requirement” can be proof of materiality; and
 - The Government paying a particular claim in full despite actual knowledge of the violation of requirements is “very strong evidence” that those requirements are not material.

Implied Certifications Lessons

- Heightened scrutiny and oversight means superheated investigatory environment.
- Have a procedure and training in place on who and what can be signed – multiple levels of approval key.
- Internal training on ethics and government contracts compliance – often mandatory under the FAR.
- Internal Oversight and “checks and balances” necessary.

Questions?



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Additional Information

FCA Whistleblower Provisions & Protections

- The FCA specifies clear and substantial Whistleblower protections - 31 U.S.C. §3730(h) prohibits retaliation against whistleblowers due to their “lawful acts” performed in furtherance of the FCA.
- Covered whistleblowers include “any employee, contractor or agent.”
- Retaliation may include: termination, discharge, hostile work environment, demotion, suspension, threat of action, harassment or “any other manner” of discriminatory conduct against one’s terms/conditions of employment.
- Relief can take the form of the Whistleblower being “made whole” and also explicitly mandates reinstatement of the employee at the same seniority status + 2 times back pay plus interest, any special damages plus attorney’s fees.
- CONFIDENTIALITY AGREEMENTS – It is illegal to have an NDA that precludes employees from having right to report FCA violations.
 - Contractor must certify to this effect – could be another FCA violation if it false certifies.

FAR 52.203-13 – Some Definitions

CONTRACTOR CODE OF BUSINESS ETHICS AND CONDUCT (JUN 2020)

(a) *Definitions. As used in this clause—*

Agent means any individual, including a director, an officer, an employee, or an independent Contractor, authorized to act on behalf of the organization.

Full cooperation-

(1) Means disclosure to the Government of the information sufficient for law enforcement to identify the nature and extent of the offense and the individuals responsible for the conduct. It includes providing timely and complete response to Government auditors' and investigators' request for documents and access to employees with information;

(2) Does not foreclose any Contractor rights arising in law, the FAR, or the terms of the contract. It does not require-

(i) A Contractor to waive its attorney-client privilege or the protections afforded by the attorney work product doctrine; or

(ii) Any officer, director, owner, or employee of the Contractor, including a sole proprietor, to waive his or her attorney client privilege or Fifth Amendment rights; and

(3) Does not restrict a Contractor from-

(i) Conducting an internal investigation; or

(ii) Defending a proceeding or dispute arising under the contract or related to a potential or disclosed violation.

Principal means an officer, director, owner, partner, or a person having primary management or supervisory responsibilities within a business entity (e.g., general manager; plant manager; head of a division or business segment; and similar positions).

FAR 52.203-13 – Some Definitions

(b) *Code of business ethics and conduct.* (1) Within 30 days after contract award, unless the Contracting Officer establishes a longer time period, the Contractor shall-

(i) Have a written code of business ethics and conduct; and

(ii) Make a copy of the code available to each employee engaged in performance of the contract.

(2) *The Contractor shall-*

(i) Exercise due diligence to prevent and detect criminal conduct; and

(ii) Otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.

(3) (i) The Contractor shall timely disclose, in writing, to the agency Office of the Inspector General (OIG), with a copy to the Contracting Officer, whenever, in connection with the award, performance, or closeout of this contract or any subcontract thereunder, the Contractor has credible evidence that a principal, employee, agent, or subcontractor of the Contractor has committed-

(A) A violation of Federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations found in Title 18 of the United States Code; or

(B) A violation of the civil False Claims Act ([31 U.S.C. 3729-3733](#)).

(c) Business ethics awareness and compliance program and internal control system. This paragraph (c) does not apply if the Contractor has represented itself as a small business concern pursuant to the award of this contract or if this contract is for the acquisition of a commercial item as defined at FAR [2.101](#). The Contractor shall establish the following within 90 days after contract award, unless the Contracting Officer establishes a longer time period:

(1) An ongoing business ethics awareness and compliance program.

(i) This program shall include reasonable steps to communicate periodically and in a practical manner the Contractor's standards and procedures and other aspects of the Contractor's business ethics awareness and compliance program and internal control system, by conducting effective training programs and otherwise disseminating information appropriate to an individual's respective roles and responsibilities.

(ii) The training conducted under this program shall be provided to the Contractor's principals and employees, and as appropriate, the Contractor's agents and subcontractors.

- (2) An internal control system.
 - (i) The Contractor's internal control system shall—
 - (A) Establish standards and procedures to facilitate timely discovery of improper conduct in connection with Government contracts; and
 - (B) Ensure corrective measures are promptly instituted and carried out.
 - (ii) At a minimum, the Contractor's internal control system shall provide for the following:
 - (A) Assignment of responsibility at a sufficiently high level and adequate resources to ensure effectiveness of the business ethics awareness and compliance program and internal control system.
 - (B) Reasonable efforts not to include an individual as a principal, whom due diligence would have exposed as having engaged in conduct that is in conflict with the Contractor's code of business ethics and conduct.
 - (C) Periodic reviews of company business practices, procedures, policies, and internal controls for compliance with the Contractor's code of business ethics and conduct and the special requirements of Government contracting, including-

- (1) Monitoring and auditing to detect criminal conduct;
 - (2) Periodic evaluation of the effectiveness of the business ethics awareness and compliance program and internal control system, especially if criminal conduct has been detected; and
 - (3) Periodic assessment of the risk of criminal conduct, with appropriate steps to design, implement, or modify the business ethics awareness and compliance program and the internal control system as necessary to reduce the risk of criminal conduct identified through this process.
- (D) An internal reporting mechanism, such as a hotline, which allows for anonymity or confidentiality, by which employees may report suspected instances of improper conduct, and instructions that encourage employees to make such reports.
- (E) Disciplinary action for improper conduct or for failing to take reasonable steps to prevent or detect improper conduct.
- (F) Timely disclosure, in writing, to the agency OIG, with a copy to the Contracting Officer, whenever, in connection with the award, performance, or closeout of any Government contract performed by the Contractor or a subcontract thereunder, the Contractor has credible evidence that a principal, employee, agent, or subcontractor of the Contractor has committed a violation of Federal criminal law involving fraud, conflict of interest, bribery, or gratuity violations found in Title 18 U.S.C. or a violation of the civil False Claims Act (31 U.S.C. 3729-3733).

(G) Full cooperation with any Government agencies responsible for audits, investigations, or corrective actions.

(d) *Subcontracts*. (1) The Contractor shall include the substance of this clause, including this paragraph (d), in subcontracts that exceed the threshold specified in FAR [3.1004](#)(a) on the date of subcontract award and a performance period of more than 120 days.

(2) In altering this clause to identify the appropriate parties, all disclosures of violation of the civil False Claims Act or of Federal criminal law shall be directed to the agency Office of the Inspector General, with a copy to the Contracting Officer.

FCA & Implied Certification – *Escobar*

- State health agency certified monthly pay apps
- Agency received payments from Federal Government
- Plaintiffs' daughter sought medical treatment and subsequently died due to adverse medicine reaction
- *Qui Tam* by parents alleged that implicit in each agency payment application was that its employees were licensed medical professionals.
 - They were not.
- Agency alleged that this was not part of express certification so FCA did not apply.

FCA & Implied Certification – *Escobar*

- U.S. Supreme Court in *unanimous* decision (Justice Thomas) ruled:
 - Implied False Certification can exist when a party:
 1. Seeking payment “makes specific representations about the goods or services provided,” and
 2. Does not “disclose noncompliance with material statutory, regulatory, or contractual requirements [and] makes those representations misleading half-truths.”
 - Misrepresentation must be material to Government’s payment analysis.

GENENTECH INC; ROCHE GROUP;
HOFFMAN LA ROCHE, INC.; ROCHE HOLDINGS, LTD.; [a]
F HOFFMAN - LA ROCHE, LTD

On Appeal from the United States District Court
for the District of New Jersey
(D.C. No. 2-11-cv-03691)
District Judge: Honorable Madeline C. Arleo

Argued November 1, 2016
Before: HARDIMAN and SCIRICA, *Circuit Judges*,
and ROSENTHAL, * *District Judge*.

(Filed: May 1, 2017)

What Other Circuits Are Saying

In holding that Petratos did not sufficiently plead materiality, we now join the many other federal courts that have recognized the heightened materiality standard after *Universal Health Services*. See, e.g., *United States ex rel. Kelly v. Serco, Inc.*, 2017 WL 117154, at *6–7 (9th Cir. Jan. 12, 2017); *Sanford-Brown*, 840 F.3d at 447; *City of Chicago v. Purdue Pharma L.P.*, 2016 WL 5477522, at *15 (N.D. Ill. Sept. 29, 2016); *United States ex rel. Scharff v. Camelot Counseling*, 2016 WL 5416494, at *8 (S.D.N.Y. Sept. 28, 2016); *United States v. N. Adult Daily Health Care Ctr.*, 205 F. Supp. 3d 276, 295–96 (E.D.N.Y. 2016); *Knudsen v. Sprint Commc'ns Co.*, 2016 WL 4548924, at *12–13 (N.D. Cal. Sept. 1, 2016); cf. *Escobar*, 842 F.3d at 111 (finding FCA violations material where those violations were “as central to the bargain as the United States ordering and paying for a shipment of guns, only to later discover that the guns were incapable of firing”).

What Other Courts Have Said

Just last year in *Universal Health Services v. United States ex rel. Escobar*, the Supreme Court confirmed that “[a] misrepresentation about compliance with a statutory, regulatory, or contractual requirement must be material to the Government’s payment decision in order to be actionable under the False Claims Act.” 136 S. Ct. 1989, 1996 (2016). The Court described this standard as “demanding” and “rigorous,” *id.* at 2002–03, and explained that a material misrepresentation is one that goes “to the very essence of the bargain,” *id.* at 2003 n.5 (citations omitted). This requirement helps ensure that the False Claims Act does not become “an all-purpose antifraud statute or a vehicle for punishing garden-variety breaches of contract.” *Id.* at 2003 (citation and internal quotation marks omitted).

What Other Circuits Are Saying

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